

Report  
of the  
Examination of  
Stockholm Town Mutual Insurance Company  
Stockholm, Wisconsin  
As of December 31, 2001

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# State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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May 10, 2002

Honorable Connie L. O'Connell  
Commissioner of Insurance  
State of Wisconsin  
121 East Wilson Street  
Madison, Wisconsin 53702

Commissioner:

In accordance with your instructions, an examination has been performed as of December 31, 2001, of the affairs and financial condition of

STOCKHOLM TOWN MUTUAL INSURANCE COMPANY  
Stockholm, Wisconsin

and the following report thereon is respectfully submitted:

## I. INTRODUCTION

The last examination of this company was made in 1997 as of December 31, 1996. The current examination covered the intervening time period ending December 31, 2001, and included a review of such subsequent transactions deemed essential to complete this examination.

The Summary of Examination Results contains elaboration on all areas of the company's operations. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The company was originally organized as a town mutual insurance company on March 23, 1872, under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Stockholm Town Insurance Company. Subsequent amendments to the company's articles and bylaws changed the company's name to that presently used.

During the period under examination, there were no amendments to the articles of incorporation and no amendments to the bylaws.

A review of the certificate of authority revealed that the company is currently licensed to write business in the following counties:

Dunn, Pepin, Pierce, and St. Croix.

The company is currently licensed to write property, including windstorm and hail, and non-property insurance.

A review was made of the policy and application forms currently used by the company. The company issues an approved policy with or without endorsements for terms of one and three years with premiums payable on the advance premium basis. Policy fees are not charged to policyholders by the company.

Business of the company is acquired through six agents, four of whom are directors of the company. Non-director agents are presently compensated for their services as follows:

| Type of Policy                | Compensation |         |
|-------------------------------|--------------|---------|
|                               | New          | Renewal |
| Homeowner, Dwelling Insurance | 15%          | 10%     |
| Liability Insurance           | 15%          | 15%     |

Director agents receive \$10.00 an hour and are reimbursed at \$.325 a mile for selling everything but liability insurance.

Agents have authority to adjust losses up to \$10,000. Losses in excess of this amount are adjusted by at least one member of the adjusters committee and the agent. Agent adjusters and other adjusters receive \$10.00 per hour for each loss adjusted plus \$.325 per mile for travel allowance.

Policyholders may participate in the management and control of the company by attending and voting at all annual or special meetings of the members. No member may vote by proxy. The annual meeting of the company for the election of directors and special meetings of the company are held in accordance with its articles of incorporation.

### **Board of Directors**

The board of directors consists of nine members divided into three classes. One class is elected at each annual meeting for a term of three years. Vacancies on the board may be filled by the directors for the interim to the next annual meeting when a director shall be chosen for the unexpired term.

The current board of directors consists of the following policyholders of the company:

| Name              | Principal Occupation | Residence     | Expiry |
|-------------------|----------------------|---------------|--------|
| William Boher *   | Salesman             | Stockholm, WI | 2002   |
| James Dettling    | Retired              | Plum City, WI | 2002   |
| John Krings       | Farmer               | Arkansaw, WI  | 2002   |
| Willard Johnson * | Retired              | Pepin, WI     | 2003   |
| Brian Rundquist   | Farmer               | Pepin, WI     | 2003   |
| Neil Solveson     | Retired              | Plum City, WI | 2003   |
| Ronald Gray       | Farmer               | Red Wing MN   | 2004   |
| Lowell Hoffman *  | Retired              | Plum City, WI | 2004   |
| P. Leland Skog *  | County Treasurer     | Bay City, WI  | 2004   |

Directors who are also agents are identified with an asterisk.

Members of the board currently receive \$30.00 for each meeting attended and \$.325 per mile for travel expenses.

### **Officers**

Officers are elected by the board of directors from among its members and hold office for one year or until their successors are duly elected and qualified.

Officers serving at the present time are as follows:

| <b>Name</b>     | <b>Office</b>  | <b>2001 Salary</b> |
|-----------------|----------------|--------------------|
| Ronald Gray     | President      | \$ 590.00          |
| John Krings     | Vice President | 722.50             |
| Willard Johnson | Secretary      | 2,610.00           |
| Lowell Hoffman  | Treasurer      | 2,922.00           |
| Maxine Johnson  | Manager        | 6,600.00           |

### **Committees of the Board**

The company's bylaws allow for the formation of certain committees by the board of directors.

The committees at the time of the examination are listed below:

#### **Adjusting Committee**

Neil Solveson, Chairman  
John Krings  
Jim Detting

#### **Investment Committee**

Lowell Hoffman, Treasurer, Chairman  
Willard Johnson  
William Bohrer

## Growth of Company

The growth of the company during the past five years as compiled from its filed annual statements was as follows:

| Year | Net Premiums Earned | Net Losses and LAE Incurred | Policies In Force | Net Income | Admitted Assets | Policyholders' Surplus |
|------|---------------------|-----------------------------|-------------------|------------|-----------------|------------------------|
| 1997 | \$202,435           | \$169,868                   | 962               | \$ 41,340  | \$1,573,214     | \$1,297,580            |
| 1998 | 171,850             | 232,584                     | 952               | (53,808)   | 1,547,969       | 1,280,546              |
| 1999 | 179,188             | 191,306                     | 936               | 1,987      | 1,557,799       | 1,269,390              |
| 2000 | 188,743             | 94,929                      | 920               | 83,090     | 1,682,558       | 1,406,571              |
| 2001 | 200,438             | 214,885                     | 912               | (12,134)   | 1,631,061       | 1,384,773              |

The ratios of premiums written, gross and net, to surplus as regards policyholders during the past five years were as follows:

| Year | Gross Premiums Written | Net Premiums Written | Ending Surplus | Writings Ratios Gross | Net |
|------|------------------------|----------------------|----------------|-----------------------|-----|
| 1997 | \$377,864              | \$210,336            | \$1,297,580    | 29%                   | 16% |
| 1998 | 398,349                | 179,822              | 1,280,546      | 31                    | 14  |
| 1999 | 435,525                | 191,827              | 1,269,390      | 34                    | 15  |
| 2000 | 432,009                | 188,636              | 1,406,571      | 31                    | 13  |
| 2001 | 436,574                | 202,935              | 1,384,773      | 32                    | 15  |

For the same period, the company's operating ratios were as follows:

| Year | Net Losses and LAE Incurred | Other Underwriting Expenses Incurred | Net Earned Premiums | Loss Ratio | Expense Ratio | Composite Ratio |
|------|-----------------------------|--------------------------------------|---------------------|------------|---------------|-----------------|
| 1997 | \$169,868                   | \$53,106                             | \$202,435           | 84%        | 25%           | 109%            |
| 1998 | 232,584                     | 59,413                               | 171,850             | 135        | 33            | 168             |
| 1999 | 191,306                     | 47,118                               | 179,188             | 107        | 25            | 131             |
| 2000 | 94,929                      | 51,356                               | 188,743             | 50         | 27            | 78              |
| 2001 | 214,885                     | 55,576                               | 200,438             | 107        | 27            | 135             |

During the examination period, the loss ratio has ranged from 50% to 135%. The expense ratio has fluctuated from 25% to 33%. The composite ratio for 2001 was 135% and 2000 was the only year in which the ratio was under 100%. Consequently, the company has had four years with underwriting losses out of the five years under examination. The losses incurred in 1998 and 2000 were largely due to storm activity, which affected many other town mutuals in Wisconsin.

Despite the noted underwriting results, surplus increased during the examination period to \$1,384,773 at December 31, 2001, due to the company's strong surplus position relative to premiums written.

## II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed there is currently one ceding treaty. The treaty contained a proper insolvency clause and complied with s. Ins 13.09 (3), Wis. Adm. Code, concerning maximum wind loss. Company retentions of risk complied with s. Ins 13.06, Wis. Adm. Code.

|                         |   |
|-------------------------|---|
| Reinsurer:              | Wisconsin Reinsurance Corporation   |
| Effective date:         | January 1, 2002, continuous   |
| Termination provisions: | Either party may terminate this contract as of any subsequent January 1 by giving to the other party at least 90 days' advance notice in writing. |

The coverage's provided under this treaty are summarized as follows:

- |                      |   |
|----------------------|---|
| Type of contract:    | Class A - Excess of Loss  |
| Lines reinsured:     | Non-property  |
| Company's retention: | \$500 for each and every loss occurrence.   |
| Coverage:            | 100% in excess of retention including loss adjusting expense. Subject to policy limits of \$1,000,000 per occurrence, single limit, for bodily injury and property damage; \$1,000,000 split limits, in any combination of bodily injury and property damage; and, \$5,000 for medical payments per person and \$25,000 per accident. |
| Reinsurance premium: | 68% of liability premiums written.  |
- |                      |   |
|----------------------|---|
| Type of contract:    | Class B - First Surplus   |
| Lines reinsured:     | All property business   |
| Company's retention: | When the company's net retention is \$150,000 or more, the company may cede on a pro rata basis up to \$800,000. When net retention is less than \$150,000, the company may cede on a pro rata basis up to 50% of such risk. The company retains an additional 10% of losses which would otherwise be ceded under the contract. |
| Coverage:            | Pro rata share of each and every loss including LAE corresponding to the amount of the risk ceded.  |
| Reinsurance premium: | The pro rata portion of premiums corresponding to the amount of each risk ceded.  |
| Ceding commission:   | 15.0% provisional commission, with a minimum of 15% and maximum of 35% based on the loss ratio.   |
- |                      |  |
|----------------------|--|
| Type of contract:    | Excess of Loss (Class C-1)   |
| Lines reinsured:     | All property business written  |
| Company's retention: | \$25,000 for each and every risk resulting from one loss occurrence. |

|                      |  |
|----------------------|--|
| Coverage:            | 100% of each loss occurrence, excluding LAE, in excess of \$25,000 up to a maximum of \$50,000.  |
| Reinsurance premium: | Net premium written times [sum of the prior four years' losses incurred plus the current year's losses incurred divided by the total net premiums written for corresponding five-year period times 100/80ths]. Minimum rate of 6% of net premium written and maximum rate of 22.0% of net premium written. The rate for the current annual period is 16%. Deposit premium of \$46,200. |
| 4. Type of contract: | Second Excess of Loss (Class C-2)  |
| Lines reinsured:     | All property business written  |
| Company's retention: | \$75,000 for each and every risk resulting from one loss occurrence.   |
| Coverage:            | 100% of each loss occurrence, excluding LAE, in excess of \$75,000 up to a maximum of \$75,000.  |
| Reinsurance premium: | 3.0% of net premium written with a minimum premium of \$6,800.   |
| 5. Type of contract: | Aggregate Stop Loss (Class D/E)  |
| Lines reinsured:     | All business written   |
| Company's retention: | Annual aggregate losses, excluding LAE, equal to 80% of annual net premiums written.   |
| Coverage:            | 100% of annual aggregate losses, excluding LAE, in excess of retention. Minimum net retention of \$165,500.  |
| Reinsurance premium: | Rate of losses incurred divided by net premiums written for last eight years losses incurred times 100/80ths, applied to net premiums written with a minimum rate of 6% and a maximum of 25%. The rate for the current annual period is 6.78%. Minimum premium of \$17,500.  |

### III. FINANCIAL DATA

The following financial statements were filed with the Commissioner of Insurance in the company's annual statement as of December 31, 2001. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Policyholders' Surplus."

**Stockholm Town Mutual Insurance Company**  
**Statement of Assets and Liabilities**  
**As of December 31, 2001**

| <b>Assets</b>  | <b>Ledger</b>             | <b>Nonledger</b>      | <b>Not Admitted</b> | <b>Net Admitted</b>       |
|--|---------------------------|-----------------------|---------------------|---------------------------|
| Cash Deposited in Checking Account   | \$ 33,286                 | \$                    | \$                  | \$ 33,286                 |
| Cash Deposited at Interest   | 943,146                   |                       |                     | 943,146                   |
| Bonds (at Amortized Cost)  | 142,526                   |                       |                     | 142,526                   |
| Stocks or Mutual Fund Investments (at Market)                                    | 311,848                   |                       |                     | 311,848                   |
| Real Estate (Net of Accumulated Depreciation and Encumbrances)                   | 1,002                     |                       |                     | 1,002                     |
| Premiums and Agents' Balances In Course of Collection                            | 7,554                     |                       |                     | 7,554                     |
| Premiums, Agents' Balances, and Installments Booked but Deferred and Not Yet Due | 77,259                    |                       |                     | 77,259                    |
| Investment Income Due or Accrued   |                           | 9,711                 |                     | 9,711                     |
| Reinsurance Recoverable on Paid Losses and LAE                                   | 104,223                   |                       |                     | 104,223                   |
| Fire Dues Recoverable  | 240                       |                       |                     | 240                       |
| Other Assets:  |                           |                       |                     |                           |
| Federal Income Tax Refund Receivable   | 266                       |                       |                     | 266                       |
| Non-Admitted assets  | 110                       |                       | 110                 |                           |
|  | <hr/>                     | <hr/>                 | <hr/>               | <hr/>                     |
| <b>TOTALS</b>  | <b><u>\$1,621,460</u></b> | <b><u>\$9,711</u></b> | <b><u>\$110</u></b> | <b><u>\$1,631,061</u></b> |

**Liabilities and Surplus**

|                                 |                    |
|---------------------------------|--------------------|
| Net Unpaid Losses               | \$ 12,636          |
| Unpaid Loss Adjustment Expenses | 606                |
| Commissions Payable             | (1,669)            |
| Unearned Premiums               | 218,457            |
| Reinsurance Payable             | 15,307             |
| Other Liabilities:              |                    |
| Expense Related                 |                    |
| Accounts Payable                | 44                 |
| Accrued Property Taxes          | 907                |
|                                 | <hr/>              |
| TOTAL LIABILITIES               | 246,288            |
| Policyholders' Surplus          | <u>1,384,773</u>   |
| TOTAL                           | <u>\$1,631,061</u> |

Stockholm Town Mutual Insurance Company  
**Statement of Operations**  
**For the Year 2001**

|  |                   |
|--|-------------------|
| Net Premiums and Assessments Earned  | <u>\$ 200,438</u> |
| Deduct:  |                   |
| Net Losses Incurred  | 210,023           |
| Net Loss Adjustment Expenses Incurred  | 4,864             |
| Other Underwriting Expenses Incurred   | <u>55,576</u>     |
| Total Losses and Expenses Incurred   | <u>270,463</u>    |
| Net Underwriting Gain (Loss)   | <u>(70,025)</u>   |
| Net Investment Income:   |                   |
| Net Investment Income Earned   | 71,736            |
| Net Realized Capital Gains   | <u>0</u>          |
| Total Investment Income  | <u>71,736</u>     |
| Other Income:  |                   |
| Miscellaneous Income   |                   |
| All other  | <u>379</u>        |
| Total Other Income   | <u>379</u>        |
| Net Income (Loss) Before Policyholder Dividends and<br>Before Federal Income Taxes | 2,090             |
| Policyholder Refunds or Dividends  | <u>0</u>          |
| Net Income (Loss) Before Federal Income Taxes                                      | 2,090             |
| Federal Income Taxes Incurred  | <u>14,224</u>     |
| Net Income (Loss)  | <u>\$(12,134)</u> |

**Stockholm Town Mutual Insurance Company**  
**Reconciliation and Analysis of Surplus as Regards Policyholders**  
**For the five-year Period Ending December 31, 2001**

The following schedule is a reconciliation of surplus as regards policyholders during the period under examination as reported by the company in its filed annual statements:

|  | <b>1997</b>        | <b>1998</b>        | <b>1999</b>        | <b>2000</b>        | <b>2001</b>        |
|--|--------------------|--------------------|--------------------|--------------------|--------------------|
| Surplus, beginning of year               | \$1,258,472        | \$1,297,579        | \$1,280,546        | \$1,269,390        | \$1,406,571        |
| Net income                               | 41,340             | (53,808)           | 1,987              | 83,090             | (12,134)           |
| Net unrealized capital gains or (losses) | 533                | 30,076             | (13,137)           | 54,091             | (9,664)            |
| Change in non-admitted assets            | 434                | 6,699              | (6)                |                    |                    |
| Other gains and (losses) in surplus:     |                    |                    |                    |                    |                    |
| Escheatable Fund – Prior                 | (3,200)            |                    |                    |                    |                    |
| Surplus, end of year                     | <u>\$1,297,579</u> | <u>\$1,280,546</u> | <u>\$1,269,390</u> | <u>\$1,406,571</u> | <u>\$1,384,773</u> |

### Reconciliation of Policyholders' Surplus

A reconciliation of the policyholders' surplus as reported by the company in its filed annual statement and as determined by the examination is detailed in the following schedule:

|   |                 |                 |                    |
|---|-----------------|-----------------|--------------------|
| Policyholders' Surplus per<br>December 31, 2001, Annual Statement |                 |                 | \$1,384,772        |
| <b>Item</b>   | <b>Increase</b> | <b>Decrease</b> |                    |
| Unearned Premium  | \$53,540        | \$ 0            |                    |
| Total   | <u>\$53,540</u> | <u>\$ 0</u>     |                    |
| Increase to Surplus per Examination                               |                 |                 | <u>53,540</u>      |
| Policyholders' Surplus per Examination                            |                 |                 | <u>\$1,438,312</u> |

## IV. SUMMARY OF EXAMINATION RESULTS

### Compliance with Prior Examination Report Recommendations

Comments and recommendations contained in the last examination report and the action taken on them by the company are as follows:

1. Corporate Records—It is recommended that the company document in the minutes of the Board of Directors meetings approval of investments in accordance with s. Ins 6.20 (6)(h)(2), Wis. Adm. Code.

Action—Compliance

2. Corporate Records—It is suggested that the company establish an investment committee and record it and its activities in the minutes of the Board of Directors meetings.

Action—Compliance

3. Fidelity Bond and Other Insurance—It is therefore recommended that the company comply with s. Ins 13.05 (6), Wis. Adm. Code, and increase its fidelity bond coverage to the amount required.

Action—Compliance

4. Claims Adjusting—It is recommended that the adjusting committee establish formal guidelines whereby all losses are either adjusted or reviewed by the adjusting committee; such guidelines should include a dollar limit which would require participation in the adjusting by the committee.

Action—Compliance

5. Disaster Recovery Plan—It is suggested to the company that this plan be formally written and included in its directors' manual.

Action—Compliance

6. Cash and Invested Cash—It is recommended that the company establish a liability for escheatable funds, and that the company file reports in accordance with Ch. 177, Wis. Stat.

Action—Compliance

7. Stocks and Mutual Fund Investments—It is recommended that the company properly classify mutual funds as MFB, MFC, MM and MFP in accordance with town mutual annual statement instructions.

Action—Compliance

8. Net Unpaid Losses—It is recommended that the company require agents to submit complete adjusting information with each weekly loss claim submission so that accurate loss estimates can be established and adequate reserves can be established and maintained.

Action—Compliance

9. Unpaid Loss Adjustment Expenses—It is recommended that the company require its agents to submit complete adjusting information on all claims activities submitted so that accurate estimates for loss adjustment expenses can be made and maintained.

Action—Compliance

## **Current Examination Results**

### **Corporate Records**

The minutes of the annual meetings of policyholders and meetings of the board of directors and any committees thereof, were reviewed for the period under examination and also for the subsequent current period.

The minutes of the Board of Directors meetings establish that the company has appointed an adjusting committee in an attempt to comply with s. 612.13 (4), Wis. Stat. However, there is no evidence in the Board of Directors or other minutes that this committee actually meets. The purpose of the statute is to insure that the board of directors, through this committee, exercises oversight over the loss adjustment process. This report also contains a recommendation made concerning timely settlement of losses that could be corrected with this oversight. It is recommended that the Adjusting Committee document their meetings and forward them to the Board of Directors for approval to evidence compliance with s. 612.13 (4), Wis. Stat.

Biographical data relating to company officers and directors have been reported in accordance with the provisions of s. Ins 6.52, Wis. Adm. Code.

The company has executed formal written agreements with its agents. The contracts include language indicating the agent will represent the company's interest "in good faith".

### **Conflict of Interest**

In accordance with a directive of the Commissioner of Insurance, each company is required to establish a procedure for the disclosure to its board of directors of any material interest or affiliation on the part of its officers, directors, or key employees which conflicts or is likely to conflict with the official duties of such person. A part of this procedure is the annual completion of a conflict of interest questionnaire by the appropriate persons. The company has adopted such a procedure for disclosing potential conflicts of interest. Conflict of interest questionnaires were reviewed for the period under examination with no apparent conflicts being noted.

### **Fidelity Bond and Other Insurance**

The company is afforded coverage under the terms of the following bonds or contracts and has complied with s. Ins 13.05 (6), Wis. Adm. Code, which sets forth the minimum requirements for fidelity bond coverage:

| <b>Type of Coverage</b>          | <b>Coverage Limits</b>  |
|----------------------------------|---|
| Workers Compensation             | \$ 100,000 each accident<br>\$ 500,000 policy limit<br>\$ 100,000 each employee           |
| Directors and Officers Liability | \$2,000,000 \$5,000 deductible  |
| Building                         | \$ 90,000 Bldg., \$10,000 Equip.<br>\$250 deductible<br>(80% co-insurance)                |
| Commercial Liability             | \$ 100,000 general and aggregate<br>\$ 50,000 each occurrence<br>\$ 5,000 medical expense |
| Errors and Omissions             | \$1,000,000 per claim<br>\$ 1,500 deductible  |
| Fidelity Bond Coverage           | \$ 80,000 all employees   |

### **Underwriting**

The company has a written underwriting guide. The guide covers all the lines of business that the company is presently writing.

The company has a formal inspection procedure for both new and renewal business. All new applications and renewal business is inspected by committee members independent of the risk under consideration and review.

### **Claims Adjusting**

The company has an adjusting committee consisting of at least three directors as required by s. 612.13 (4), Wis. Stat. The function of this committee is to adjust or supervise the adjustment of losses. A recommendation concerning documentation of adjusting committee meeting is located in the section captioned "Corporate Records".

### **Accounts and Records**

The examiners' review of the company's records indicated that the company is in compliance with s. Ins 13.05, Wis. Adm. Code, which sets forth the minimum standards for the handling of cash and recording of cash transactions by town mutual insurance companies. The examiners noted the following:

1. A proper policy register is maintained
2. A proper cash receipts journal is maintained
3. A proper cash disbursement's journal is maintained
4. A proper general journal is maintained
5. A proper general ledger is maintained

An extensive review was made of income and disbursement items. Cash receipts were traced from source records and the proper recording and eventual deposit thereof ascertained. Negotiated checks issued during the period under examination were reviewed, test checked for proper endorsement, and traced to cash records. The verification of assets and determination of liabilities were made as of December 31, 2001.

The company is audited annually by an outside public accounting firm.

### **Disaster Recovery Plan**

A disaster recovery plan identifies steps to be performed in case the company loses a key employee, or the office building was destroyed, to name a couple of contingencies. The company has developed a disaster recovery plan. The company's disaster recovery plan appears to be adequate.

### **Invested Assets**

Section 610.23, Wis. Stat., requires insurers to hold all investments and deposits of its funds in its own name except that:

- (1) Securities kept under a custodial agreement or trust arrangement with a bank or banking and trust company may be issued in the name of a nominee of the bank or banking and trust company; and
- (2) Any insurer may acquire and hold securities in bearer form.

For securities not held under a custodial agreement or trust arrangement with a bank or banking and trust company, s. Ins 13.05 (4), Wis. Adm. Code, requires that:

Non-negotiable evidences of company investments such as registered bonds, certificates of deposits, notes, etc., shall be maintained in a safe or vault with adequate safety controls or in a safety deposit box in a bank. Negotiable evidences of company investments shall be maintained in a safety deposit box in a bank. Access to a company safety deposit box containing negotiable securities shall require the presence and signature of at least 2 officers, directors or employee's of the company.

The company is in compliance with these requirements.

### **Investment Rule Compliance**

The investment rule for a town mutual allows a company to invest in common stocks, common stock mutual funds, and other higher risk investments (referred to as "Type 2") provided that the town mutual has a sufficient amount of lower risk investments (referred to as "Type 1"). A town mutual may invest in Type 2 securities only if it already has sufficient Type 1 investments. Type 1 investments must equal or exceed the greater of items 1, 2, or 3.

|   |                   |
|---|-------------------|
| 1. Liabilities plus \$300,000                     | \$ 546,288        |
| 2. Liabilities plus 33% of gross premiums written | 408,164           |
| 3. Liabilities plus 50% of net premiums written   | 366,507           |
| 4. Amount required (greater of 1, 2, or 3)        | 546,288           |
| 5. Amount of Type 1 investments as of 12/31/2001  | <u>1,085,221</u>  |
| 6. Excess or (deficiency)                         | \$ <u>538,933</u> |

The company has sufficient Type 1 investments.

## **ASSETS**

|                               |                  |
|-------------------------------|------------------|
| <b>Cash and Invested Cash</b> | <b>\$976,432</b> |
|-------------------------------|------------------|

The above asset is comprised of the following types of cash items:

|   |                      |
|---|----------------------|
| Cash deposited in banks-checking accounts | \$ 33,286            |
| Cash deposited in banks at interest       | <u>943,146</u>       |
| <br>Total                                 | <br><u>\$976,432</u> |

Cash deposited in banks subject to the company's check and withdrawal consists of one account maintained in a local bank. Verification of checking account balances was made by obtaining confirmations directly from the depository, and reconciling the amounts shown thereon to company records.

Cash deposited in banks represents the aggregate of forty-three deposits in twelve depositories. Deposits were verified by direct correspondence with the respective depositories and by an actual count and inspection of certificates and/or passbooks. Interest received during the year 2001 totaled \$62,919 and was verified to company cash records. Rates of interest earned on cash deposits ranged from 1.75% to 7.16%. Accrued interest on cash deposits totaled \$6,693 at year-end.

|                            |                  |
|----------------------------|------------------|
| <b>Book Value of Bonds</b> | <b>\$142,526</b> |
|----------------------------|------------------|

The above asset consists of the aggregate book value of bonds held by the company as of December 31, 2001. Bonds owned by the company are located in a safety deposit box with the other investments.

Bonds were physically inspected by the examiners. Bond purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in bonds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers. An exception was granted for a bond, which was over the three-percent of assets limitation, pursuant to s. Ins. 6.20 (6) 9 (f) 1.Wis. Adm. Code.

Interest received during 2001 on bonds amounted to \$10,365 and was traced to cash receipts records. Accrued interest of \$2,527 at December 31, 2001, was checked and allowed as a non-ledger asset.

**Stocks and Mutual Fund Investments****\$311,848**

The above asset consists of the aggregate market value of stocks and mutual funds held by the company as of December 31, 2001. Stocks owned by the company are located in a safety deposit box with the other investments.

Stock certificates were physically examined by the examiners. Stock and mutual fund purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in stocks and mutual funds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Dividends received during 2001 on stocks and mutual funds amounted to \$4,944 and were traced to cash receipts records. Accrued dividends of \$491 at December 31, 2001, were checked and allowed as a non-ledger asset.

**Book Value of Real Estate****\$1,002**

The above amount represents the company's investment in real estate as of December 31, 2001. The company's real estate holdings consisted of their office building.

The required documents supporting the validity of this investment were reviewed and were in order. Adequate hazard insurance was carried on the real estate and contents as noted under the caption, "Fidelity Bond and Other Insurance." The company's investment in real estate and related items was in conformance with the Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers. Real estate depreciation is calculated using the straight-line method.

**Agents' Balances or Uncollected Premiums****\$84,813**

The above ledger asset represents the amounts due from agents or policyholders which are not in excess of 90 days past due at year-end. This balance is made up of Premiums in Course of Collection and Premiums Booked but Deferred and Not Yet Due. A review of individual agent's accounts verified the accuracy of this asset.

**Investment Income Due and Accrued****\$9,711**

Interest due and accrued on the various assets of the company at December 31, 2001, consists of the following:

|                            |            |
|----------------------------|------------|
| Cash Deposited at Interest | \$6,693    |
| Bonds                      | 2,527      |
| Stocks and Mutual Funds    | <u>491</u> |
| Total                      | \$9,711    |

**Reinsurance Recoverable on Paid Losses****\$104,223**

The above asset represents recoveries due to the company from reinsurance on losses which were paid on or prior to December 31, 2001. A review of year-end accountings with the reinsurer verified the above asset.

**Equipment, Furniture, and Supplies****\$0**

This asset consists of \$573 of equipment owned by the company and fully depreciated at December 31, 2001. In accordance with annual statement requirements, this amount has been deducted as an asset not admitted.

**Fire Department Dues Recoverable****\$240**

This asset represents the fire department dues recoverable at December 31, 2001. The examiners reviewed the company's fire department dues calculation and found this asset to be correctly calculated.

**Federal Income Taxes Receivable****\$266**

This asset represents the balance receivable at year-end for federal income taxes incurred prior to December 31, 2001.

The examiners reviewed the CPA's updated tax calculation and the amount was not materially different from the reported amount at year-end 2001.

## LIABILITIES AND SURPLUS

### Net Unpaid Losses

\$12,636

This liability represents losses incurred on or prior to December 31, 2001, and remaining unpaid as of that date. The examiners' development of unpaid losses is compared with the amount estimated by the company in the following schedule. Differences are reflected in the section of this report captioned "Reconciliation of Policyholders' Surplus."

|  | Company Estimate | Examiners' Development | Difference        |
|--|------------------|------------------------|-------------------|
| Incurred But Unpaid Losses               | \$388,200        | \$ 443,653             | (\$55,453)        |
| Less:                                    |                  |                        |                   |
| Reinsurance Recoverable on Unpaid Losses | <u>375,563</u>   | <u>429,659</u>         | <u>(54,096)</u>   |
| Net Unpaid Losses                        | <u>\$ 12,637</u> | <u>\$ 13,994</u>       | <u>(\$ 1,357)</u> |

The examiners developed this liability by totaling actual loss payments made through the development period on those losses incurred on or prior to December 31, 2001. To the actual paid loss figures was added an estimated amount for those 2001 and prior losses remaining unpaid at the examination date. The above difference of (\$1,357) was not considered material for purposes of this examination.

The examiners' review of claim files included open claims, paid claims, claims closed without payment, and all claims which were denied during the examination period. The review indicated that, except as noted below, claims are investigated and evaluated properly and that payments are made promptly and in accordance with policy provisions upon the submission of a proper proof of loss. In addition, the review of claims handling procedures and files revealed the following:

1. A proper loss register is maintained.
2. Claim files contained sufficient investigatory data and documentation to verify settlement payments or reserve estimates.
3. Proofs of loss were properly signed.

The examination also noted that the company routinely allows claims to remain open for a number of years without settlement, while waiting for information from the claimant or for the insured to repair covered damages. This practice may be interpreted to be an unfair settlement policy by failure to initiate and conclude claim investigations in a reasonable period of time. It also increases the company's exposure to additional loss sustained on damaged and unrepaired property. It is recommended that the

company adopt procedures for timely settlement of claims, in compliance with s. Ins 6.11 (3) (a) 2, Wis. Adm. Code.

**Unpaid Loss Adjustment Expenses**

**\$606**

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2001, but which remained unpaid as of year-end. The methodology used by the company in establishing this liability is combination of actual accrued and CPA estimates.

The examiners' analysis of expenses incurred in the current year related to the settlement of prior year losses, as well as estimates of amounts necessary to settle any prior losses remaining unpaid at the examination date, determined this liability to be adequately stated.

**Unearned Premiums**

**\$164,917**

This liability represents the reserve established for unearned premiums in compliance with s. Ins 13.08 (3), Wis. Adm. Code. This reserve was computed using a 50% of annualized premium, which includes deferred installments. In addition, the company added its deferred installments to this balance. This overstated unearned premiums by the additional deferred installment amount. It is recommended that the company should use the 50% of annualized premium method of computing unearned premium in compliance with s. Ins. 13.08 (3), Wis Adm Code and to not add any deferred installment estimate. This examination resulted in a \$53,540 reduction in Unearned Premium and an Increase in Surplus of the same amount.

**Reinsurance Payable**

**\$15,307**

This liability consists of amounts due to the company's reinsurer at December 31, 2001, relating to transactions which occurred on or prior to that date.

|               |                 |
|---------------|-----------------|
| Class A       | \$ 6,225        |
| Class C-1     | 3,850           |
| Class C-2     | 700             |
| Class D/E     | 1,800           |
| First Surplus | 9,245           |
| Overpayment   | (30,232)        |
| Deferred      | <u>23,719</u>   |
| Total         | <u>\$15,307</u> |

Subsequent cash receipts, disbursements, and reinsurance accountings verified the amount of this liability.

**Commissions Payable**

**(\$1,669)**

Commissions Payable (\$1,387)

|                                |                |
|--------------------------------|----------------|
| Deferred Commission Payable    | 3,276          |
| Deferred Commission Receivable | <u>(3,558)</u> |
| Total                          | (\$1,669)      |

This liability represents the amounts due to the company's agents at December 31, 2001. The examiner found this liability to be reasonably stated.

**Amounts Payable** **\$44**

This liability represents phone bills in the possession of the company at December 31, 2001. Supporting records and subsequent cash disbursements verified this item.

**Payroll Taxes Payable** **\$907**

This liability represents the company's portion of payroll taxes incurred prior to December 31, 2001, which had not yet been paid. Supporting records and subsequent cash disbursements verified this item.

## **V. CONCLUSION**

Stockholm Town Mutual Insurance Company is a town mutual insurer with an authorized territory of four counties. The company has been in business over 130 years providing property and liability insurance to its policyholders.

Since the prior examination as of December 31, 1996 the company's assets have increased 4.3% to \$1,631,061. Liabilities have decreased 19.3% to \$246,288. Surplus has increased 10.0% to \$1,384,773. The company had net losses two out of the last five years.

This examination resulted in three recommendations and an increase to surplus of \$53,540. The recommendations are listed in summary form on the following page.

## VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 12 Corporate Records—It is recommended that the Adjusting Committee document their meetings and forward them to the Board of Directors for approval to evidence compliance with s. 612.13 (4), Wis. Stat.
2. Page 19 Losses—It is recommended that the company adopt procedures for timely settlement of claims, in compliance with s. Ins 6.11 (3) (a) 2, Wis. Adm. Code.
3. Page 20 Unearned Premium—It is recommended that when computing unearned premium, the company should use the original or full term premium basis in compliance with s. Ins. 13.08 (3), Wis Adm Code and to not add any deferred installment.

## **VII. ACKNOWLEDGMENT**

The courteous cooperation extended to the examiners by the company's personnel is hereby acknowledged.

In addition to the undersigned, David Grinnell of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination:

Respectfully submitted,

Russell Lamb  
Examiner-in-Charge